Compliments of the First National Bank in Minneapolis, Minn.
Correspondent of The National City Bank of New York

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THE NATIONAL CITY BANK OF NEW YORK

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Economic Conditions
Governmental Finance
United States Securities

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European Affairs

THE past month has been an eventful one in the political affairs of Europe. The British election has confirmed the retirement of Lloyd-George from the premiership and established the Conservative party in power with a majority of about 80 in the House of Commons. The Labor party is second with less than one-half as many votes, and has the honor of being the Opposition party. This is emphasized in some quarters as significant of the growing political power of the labor element, and no doubt bears such significance, although not quite to the degree or in the sense given it by all interpreters. The Labor party has had a very considerable delegation in the House for many years, and in the opinion of most observers instead of being a disturbing element in the country's affairs its influence has been to modify and temper extreme agitation. The contact with and participation in the government has developed high qualities of leadership in some members of the group, and been a good thing for Labor and for the country. This is the opinion of many people who would not like to see the Labor party come into control.

New German Cabinet

In Germany the Wirth government has finally given up the struggle and retired. It was blamed at home for not getting better terms from the Allies, and did not command the popular strength to carry out the measures of internal reform required. Whether any other government can do better probably depends upon the extent to which the Allies will grant concessions, for it is doubtful if the drastic policies that are necessary to put the finances of Germany on a sound basis can have popular support unless accompanied by a settlement of the reparations question regarded as practical. In other words, the feeling in Germany is that no efforts will get them anywhere unless there is radical revision of the reparations demands. Meanwhile the printing of currency goes on at an ever-increasing rate, the latest valuation of the mark being approximately 8,000 to the dollar.

Great Britain and France

The new government in England is undoubtedly strong for the maintenance of friendly relations with France, but practically all public opinion in England is favorable to a new deal with Germany. The new premier, Mr. Law, has given out that the Balfour announcement of last August, that Great Britain cannot consider concessions upon the allied debts to it unless the United States will consider concessions upon Britain's indebtedness to this country, may be reconsidered. Moreover, there are evidences of growing opinion in France that a readjustment of terms and suspension of cash payments may be necessary. There is a basis for this feeling in an improvement in industrial and financial conditions in France. Public revenues are increasing, industry in the war-occupied regions is gaining, the public response to new government loans is very gratifying and the national credit shows signs of abundant strength. Although the note issues of the Bank of France showed an increase in the early Fall, this has since been retired, and the debt of the government to the Bank is now at the lowest point since the war. In short, the French people, instead of being discouraged and desperate, have increasing confidence in their ability to deal with the situation. Although this does not imply a disposition to abandon claims upon Germany, it indicates France is not wholly dependent upon reparations and is favorable to an amicable understanding with England.

New Cabinet in Italy

Italy is another country in which a change of administration has occurred, the Fascisti, a patriotic society originally formed to combat the disorderly activities of socialists and communists, having come into complete control of the government, with its head, Mussolini, as Prime Minister. Although believers in constitutional government are not disposed to look with favor upon spontaneous and irregular movements to promote even the best of causes, the Fascisti have given evidence of high patriotic purposes, and Mussolini's declarations of policy are such as to inspire confidence that

order and good government will be maintained at home and the relations of Italy with other countries will be on a friendly basis.

Before the war Mussolini was the editor of a socialist paper, but the extremists of socialism developed his ideas in the other direction. He is quoted as saying that there are about three times as many employes on the Italian state railways as there ought to be, and that in order to obtain efficient management for the railways, telegraphs and telephones they should be turned over to private companies, thus relieving the national treasury of the heavy drain they are now causing. Although the Fascisti did not come into power as the result of a popular election, the public appears to be pleased with it. Mussolini says that an election will be held shortly.

Reform in Austria

In Austria, the bill to carry out the plan adopted by the League of Nations for the reorganization of the government and finances is now being debated in the parliament. The measure is very drastic in many respects, particularly in readjusting the organization of the government to the reduced size and revenues of the country, and cutting down expenditures. It is said that 100,000 government employes will be lopped off, but this is accomplished in part by turning over many public services, such as the railroads, telegraphs and telephones to public service stock companies, which will be under private management, and under the necessity of supporting themselves instead of living on subsidies from the public treasury, as heretofore. The plan contemplates a resolute attempt to make revenues and expenditures balance. The responsibility of issuing currency will be turned over to a central banking institution, operated by private capital, like the Federal Reserve system of the United States, so that currency issues will be absolutely divorced from the government finances.

This reads like a decidedly drastic program to be adopted by a parliamentary body in which socialism is said to be dominant, but it represents a return to sound principles, and apparently Austria has had enough of the other kind to appreciate a change.

Domestic Political Conditions

In this country an election has been held which seems to have strengthened the reactionary element at Washington. This is not applying the term "reactionary" as it has been commonly used, but as seems to be appropriate in this instance. It refers to a political group which fought the recent campaign over the "great deflation" of 1920-21, without regard to the fact that the country already has travelled a long way on the road of recovery from the depressing conditions of those years.

Periods of business depression have occurred from time to time, ever since industry and business became organized to such a degree that people, instead of supplying all their own wants have exchanged goods and services, and thus become dependent upon each other. As industry has become more highly specialized, bringing the people of all countries into trading relations, and particularly as the use of credit has developed, these periods have become more pronounced and demoralizing. They are due fundamentally to the fact that a complicated organization is more likely to get out of order than one of few parts. These conditions are fully recognized by the economists of all countries, and by practical people of experience.

Such people understand that these periods of disturbance are disastrous to all business, because they reduce the volume of the exchanges and curtail the earnings of every kind of business.

In every such period of disturbance there are two classes of people, to wit: those who quickly recognize that one of the readjustments to which the system is subject is under way, that the normal balance in the exchanges has been disturbed, and that individuals must adjust themselves to the general situation; and, on the other hand, those who forthwith conclude that some mysterious and pernicious influence is at work of which they are the chosen victims. This hallucination is the natural successor in primitive minds of the once common belief that invisible spirits ruled over the fortunes of men. It used to be thought that nothing ever happened to a man that had not been brought about by these spirits, and it was thought well to retain the services of a "medicine man" of some sort who was able to deal with them. These "medicine men" have their successors in some of the politicians of the present day, and the faith in incantations is very well illustrated by faith in the legislation commonly proposed for the relief of business depression.

The Fall of Prices 1920-21

The fall of prices and business crisis of 1920-21 took place all over the world. It was not unforeseen or unpredicted, although the exact time when it would occur could not be definitely calculated. Warnings in abundance had been uttered, and nearly all men of business experience knew that the wild race between wages and prices could not go on indefinitely, and that whenever prices ceased to rise they would begin to fall. It did not require a soothsayer or medicine man to foretell that a level of prices brought about by the great war would not be permanently main-

tained after the war was over. Nevertheless, comparatively few people had their houses in order when the inevitable readjustment came.

The late campaign has been waged in some sections of the country upon the theory that the markets have been manipulated against the farmers. It has been alleged that the grain and cotton exchanges were agencies by means of which the deflation of prices was engineered, but the articles traded in on the exchange fell more slowly than many other commodities. The first decline in farm products was in meat and live stock. In the fiscal year ended June 30, 1919, the exports of meats from the United States aggregated 3,338,000,000 pounds, and in the following year, ended June 30, 1920, they dropped to 2,048,000,000 pounds, or a little more than one-third. This was a disturbance in the markets for meats and meat animals, and in the feeding season of 1919-20 the farmers lost money on cattle and hogs. All live stock reached the highest prices in 1919, and began to decline before the general decline of grains, cotton and other commodities. In the fiscal year ended June 30, 1921, meat exports fell to 823,000,000 pounds, the lowest total of our meat exports in more than 20 years, and less than one-fourth the total of the fiscal year 1918-19. This falling off might be supposed to have something to do with the decline of live stock values, but the political soothsayers put the responsibility upon Wall Street.

The first country to experience the decline of prices so acutely as to cause a crisis was Japan, in March, 1921, and the immediate cause was a falling off in the demand for silk. Japan's chief export commodity. The rise of prices had begun to pinch a great many people; the income of a great many people did not increase in corresponding degree. The industrial situation was losing the balanced relationship which is necessary to prosperity. Silk was one of the first commodities to reflect enforced economy. In a few months, however, the effects were visible in goods of more common consumption. The spring trade of 1920 was a disappointment to merchants; the keen ones sensed the situation, price-cutting began, and in May came the torrent of order-cancellations in woolen and cotton goods, shoes and other goods. Even yet, the principal farm products, excepting live stock, were not affected. Wheat sold as high as $3.45 per bushel in May, $3.00 in July and $2.74 in September, while cotton touched the high point of the war and post-war period in July, at 43.75 cents per pound.

Credit Inflation and Deflation

It is appropriate in this connection to again call attention to the work of the Joint Committee of Agricultural Inquiry, appointed by Congress in the fore part of 1921, to make a searching investigation into banking and credit conditions, with particular reference to the deflation of credit and agricultural prices. The Commission* has among its membership several members of the agricultural bloc, notably the present head of the group, but although the Commission has issued several volumes of reports, its findings are seldom mentioned by the agitators. They have continued to affirm what the Commission finds to be untrue.

Part II of the Report consists of a review of the policy of the Federal Reserve banks during and preceding the crisis. The Commission sums up its conclusions as follows:

1. That the expansion of bank loans in rural districts during the period of inflation ending June, 1920, was relatively greater than in the industrial sections, taken as a whole.
2. That the action of the Federal Reserve Board and the Federal reserve banks during the 15 months preceding April 28, 1921, did not produce a greater curtailment of bank loans in the rural districts than in the financial and industrial sections.
3. Credit was not absorbed by the financial centers at the expense of rural communities for the purpose of speculative activities.
4. That the pressure of the forces of liquidation and depression in the agricultural sections was reflected in a reduction of deposits. This reduction of deposits, particularly demand deposits, was relatively larger in the agricultural and semi-agricultural counties in the United States than in the industrial counties.†

This report is signed by all the members of the Commission.

World Influences

Approximately 15 per cent of the gross agricultural production of the United States, as shown by official calculations, must find consumption abroad or remain as surplus at home. Under these conditions it would seem to be apparent that anything seriously affecting industrial conditions abroad and the ability of foreign peoples to buy our products must affect markets and prices in this country. It is common knowledge that the whole world has

* The members of the Agricultural Joint Commission for the Senate, are Lenroot, of Wisconsin; Capper, of Kansas; McNary, of Oregon; Robinson, of Arkansas; Harrison, of Mississippi. The members for the House are Anderson, of Minnesota, Chairman; Mills, of New York; Funk, Illinois; Sumner, Texas; TenEyck, New York.

† On pages 650 and 651 of the Hearings appear data submitted by Governor Strong showing relative progress of agricultural and industrial liquidation from May 4, 1920, to April 28, 1921. The data are obtained from analysis of reports to the Comptroller of the Currency and the Federal Reserve Board from about 9,500 banks throughout the country which are members of the Federal Reserve System. It is shown that during this period, during which the most serious credit strain occurred. loans by the Reserve banks to member banks in agricultural communities **increased** 57 per cent. Loans to members in semi-agricultural communities decreased .2 per cent, while those to members in industrial communities **decreased** 29 per cent. These figures are refutation of the charge that Reserve banks practised discrimination against agricultural districts.

been passing through a crisis and that the per capita consumption of imported foodstuffs by the countries of Europe has been very much reduced. They are buying with the most careful economy. Moreover, the prices of foodstuffs and natural products generally have fallen in all countries quite as much as they have in the United States.

The Menace of Reactionary-Radical Policies

Notwithstanding the evidence that the depression of agricultural prices has been directly related to the world situation, policies are proposed in the name of relief for agriculture, which if carried out must tend to check the improvement in agricultural conditions which is under way, and throw the country back into a state of disorganization, uncertainty and confusion.

The stock market, which is quick to sense developments unfavorable to orderly business progress, has shown decided weakness since the election, railroad shares leading in the decline. Although the country evidently is suffering from the inadequacy of railroad facilities, due to the fact that railroad investments no longer command the confidence of the public, one of the objects of the revived agiitation is the repeal of the transportation act defining what, in the opinion of the legislative authority, is a fair return upon railroad property. Nothing more would be required to make the railroad situation hopeless. Railroad service cannot be had without the facilities, and these cannot be had unless the investing public is assured of a return corresponding to what can be had in other fields of investment. One view commonly held at the sources of this agitation seems to be that the railroads are owned by a few rich bankers who are able to put their hands in their pockets for all the money needed to provide the necessary expansion of service. The railroads, however, are not owned by bankers; the ownership is widely distributed and will respond with additional capital only as it believes the investment to be safe. The strongest companies are able to borrow, by giving mortgages or obligations that rank ahead of their stock, but this is just like putting a second mortgage on a farm. This process cannot be carried indefinitely, because the margin of safety grows smaller. Proper financing of the railroads requires that approximately one-half of the capital shall be represented by capital stock; in other words, that proportion should be proprietary capital, in order to obtain favorable terms upon borrowed money. Very little new capital has been raised for railroads by that means recently.* Expenditures for rolling stock are financed mainly by means of equipment trusts, the new equipment being mortgaged for about 75 per cent of its cost.

General Business Conditions

The political developments of the month, while disquieting to the extent indicated above, are not of immediate influence, and one of the reasons for regretting them is that the natural tendencies of the time are good. The advance of agricultural prices has put new life into business in sections where depression has existed, and the volume of business being done in most lines, in all parts of the country is now very satisfactory. As a rule prices of manufactures have not advanced enough to cover the advances in wages and raw materials, with the result that complaints of little or no profits are common.

The iron and steel industry is going at about 80 per cent of capacity, and making headway upon bookings accumulated during the strikes. Pig iron is lower as a result of the resumption of numerous furnaces, and prices are weaker in several lines. The future is hopefully viewed, on the strength of buying by the railroads, prospects for another year of activity in construction work, better outlook for implements and great confidence among automobile manufacturers.

The textile industries have been stimulated by the rise of raw materials, all of which are regarded in strong position, and are more completely employed than for more than two years. The strikes, some of which have

* Volume II of "Income in the United States," by the National Bureau of Economic Research, Inc., has been issued recently. The organization which has conducted this study, has made an impartial, scientific study of the distribution of annual income in this country, and the results are the most trustworthy to be had. From Chapter 9, of Volume II, devoted to railroad income and distribution, page 131, we quote the following which sums up the results of its studies down to 1918. Since 1918 the position of railroad employes has further improved, and the position of security holders has relatively receded:

"The figures in table 91 show that the average annual compensation paid by railways to their employees has risen materially since 1909, the increase up to 1918, when measured in purchasing power, amounting to something over 30 per cent. During this period, therefore, the increase in money earnings more than kept pace witn the rise in the value of commodities consumed by the working classes. The facts brought out do not show, however, whether this increase in earning power has resulted from monopolistic organization of wage earners, from increased efficiency of the wage earners, from an increase in the supply of railway equipment as compared to railway laborers, from a general increase in the wage level, or from some entirely different cause.

"The purchasing power of the total share of the security holders increased rather steadily up to 1914, but since that date, has fallen materially, until in 1918, it was smaller than in 1909. This change in the total tells nothing concerning the income per dollar invested. Since, however, it is believed that the total investment in the railway business has been increasing, it appears that the recent decline in the total income of the security holders must have been accompanied by a considerably greater fall in the returns per unit of investment."

dragged along from last February to recent weeks, have all been settled, the outcome in most cases being victory for the employes, in the sense that they were successful in resisting the demands of the employers for wage-reductions and return to the nine-hour day. The Amoskeag Company, of New Hampshire, was successful in re-establishing the longer day, but rescinded its demand for a 20 per cent reduction of wages. The other companies yielded both on hours and wages. It should be said in this connection that market conditions have improved very much from what they were when the mills undertook to put the reductions into effect. The curtailment of production resulting from the strikes has been an important factor in stiffening the price of cotton goods, and the short crop of cotton has influenced dealers to buy more freely despite price advances. At present, the industry is active, although producers still claim that goods have not risen enough to cover advancing costs, and that their profits are being realized on raw material bought at lower than present prices.

Conditions in Cuba have made a very satisfactory recovery this year. Contrary to apprehensions a year ago, the sugar crop of 1921-22 (although nearly 4,000,000 tons), has been absorbed, and prices have advanced to just under 4 cents per pound. Grinding on the new crop will begin shortly, and it is expected that the yield will be about the same as for the last year. At the present price the crop will yield good profits to growers, and go far toward putting the industry in good condition. Cuba when prosperous is an important market for the United States, and the situation there is very encouraging.

On the whole the outlook for business during the Winter months is good, with a promise of continuance next Spring, providing developments in Europe are not unfavorable, and that the rise of prices in other lines does not offset the rise that has taken place in farm products. The fact cannot be neglected that the prices of farm products are dependent upon Europe's taking its accustomed supplies, and that prosperity cannot be maintained unless the farmer has a share in it. The census figures just published show 31,614,269 persons actually living on farms in this country, and there are a great many more living in towns directly dependent upon the trade with farmers. It is useless to expect that the cotton and woolen industries, clothing and shoe trades, or any other of the leading industries will be able to run full if these people are obliged to curtail their purchases as has been the case for the past year. Farm products have had an encouraging rise in recent weeks, but the value of it is being offset by the advances now taking place in what the farmers have to buy.

The improved conditions in the industries still partakes largely of the nature of a rally from the extreme depression and low production of 1921. Many experienced observers do not believe that industrial costs are low enough to furnish the basis for permanent prosperity.

The Agricultural Situation

The November estimates of the Department of Agriculture, upon the crops of the past season are given below, in comparison with the final estimates for 1921, and the average for the five years, 1916-20:

PRODUCTION (000 omitted)

Crops	1922 (Preliminary)	1921 (Dec. estimate)	1916-20 average
Corn, bus.	2,896,108	3,080,372	2,830,942
Wheat, bus.	810,1[illegible]3	794,893	799,083
Oats, bus.	1,229,774	1,060,737	1,412,602
Barley, bus.	196,431	151,181	197,447
Rye, bus.	79,6[illegible]3	57,918	67,762
Buckwheat, bus.	13,643	14,079	14,426
Potatoes, bus.	433 905	346,8 3	373 417
Sw. potatoes, bus.	110,359	98,660	88,750
Hay, all tons	108,736	96,802	102,129
Cotton, bales	10,135	7,954	11,931
Flaxseed, bus.	12,101	8,112	10,972
Rice, bus.	39,159	36,515	41,651
Sugar beets, tons	5,000	7,782	6,623
Kafirs (7 states), bus.	81,488	115,110	91,330
Beans (7 states), bus.	13,013	9,118	13,317
Broom Corn (7 states), tons	32	35	50
Cloveseed, bus.	1,878	1,411	1,564
Peanuts, lbs.	691,057	816,465	1,043,292

The price index of all crops on November 1 was 17.2 per cent more than a year ago and 40.2 per cent less than the average of the preceding five years. The production index is about 12.0 per cent more than last year's aggregate production and 0.3 per cent more than the average of the preceding five years 1916-1920.

The estimate for corn is higher than that of the previous month, and including the carry-over gives a total available supply for the coming year of 3,084,000,000, or about the amount of last year's crop, saying nothing of carry-over. Considering that there are more hogs on the farms, and a much greater number of cattle in feed lots than a year ago, the position of corn is very strong. The way the record-breaking crop and carry-over of last year has been disposed of augurs well for the corn-growers in the future. Calculations indicate that approximately 3,200,000,000 bushels of corn were consumed in this country or exported last year and there never has been but one crop of that size in the history of the country, and but four crops exceeding 3,000,000,000 bushels. The price in Chicago is about 70 cents per bushel, and at western railroad stations about double the price of a year ago.

Wheat is in a strong position, statistically, in view of the poor crops of bread grains in

Europe. The normal pre-war wheat production of France was about 325,000,000 bushels, and the normal annual consumption is 340,000,000 to 345,000,000 bushels. A saving of 14,000,000 bushels is expected from the milling regulations, requiring "war flour" to be used, but the import requirements are calculated at about 80,000,000 bushels. In Germany the crops of all the grains are very deficient, and vigorous measures are being taken to conserve supplies. The feeding of bread grains to cattle is forbidden, and also the use of barley for making strong beer. The supply of potatoes is reported good, except in Saxony. Poland and the Balkan countries have little grain for export; Russia, none. The crop of Argentina is larger than at first reported, but the Australian crop will be less. The United States and Canada are the main dependence. The situation is summed up by J. E. Hay, Canadian Trade Commissioner at Manchester, England, as follows:

The marketing of wheat in the future will be characterized by much uncertainty regarding consumption and prices. Many countries in the continent of Europe will be sorely in need of wheat, but it is not known how they can possibly pay for it. If shippers are reluctant to export to countries with dubious funds, naturally there will be so much the larger quantity on offer to countries whose credit is sound, with the consequent effect upon prices.

The fact that prices for the May delivery of wheat are about the same as for December, shows the indisposition to speculate in the futures.

Grain Congestion

The marketing situation in the west has been complicated by a congestion of offerings at the country railway stations beyond the ability of the railroads to handle it. The congestion seems to have been the worst ever known, over 400 country elevators in Kansas being at one time closed because their bins were full. But the congestion has not been simply at the railroad stations in the west, but all along the route to the seaboard. The situation has been graphically described recently by Mr. Julius H. Barnes, President of the Chamber of Commerce of the United States, and a member of one of the leading firms in the grain trade at Duluth and New York. He was talking before a public meeting in New York about maintaining the railroads of the country in effective condition and affording the means for increasing their facilities, when he adverted to the grain situation as follows:

You will agree with me that if there is one single menace to the onward march of business activity and prosperity in this country it rests in the dissimilarity between the prices paid for farm products and the prices of these commodities which the farmers must buy.

I do not follow the full way with those who say that the farm is in a state of collapse. It is no such thing. Twenty cent cotton and ten dollar hogs will take care of a large part of our farmers with a measure of prosperity, but the grain-raising country has suffered and the grain-raising country has today the sunrise of hope before it.

Yet this is the situation: From the first of September until the first of October, in the very height of the crop-moving period of this country, the main channel of export outlet for grain in America, from Buffalo to New York, was practically closed. For thirty days the four great trunk lines that serve that channel of movement contracted no grain for movement. The grain moved from the West until it had congested and exhausted the elevator facilities of Buffalo—18,000,000 bushels. As soon as the unloading facilities were thus exhausted, the lake carriers, reflecting the apprehension of their owners that the boats would be tied up with undischarged cargoes instead of being returned, made an advance in the lake rates, in 30 days from 2 cents per bushel for the carrying of grain from Chicago and Duluth to Buffalo, to 6 cents.

The rail rate from Buffalo to New York, on the published tariff, is nine cents, but as I explained to your practically no grain was moving. The route that was open—the Erie Canal—with totally inadequate facilities, advanced the rate to 13 cents per bushel, paralleling the railroad, which was supposed to carry it for 9.

From Buffalo to Montreal is a water route. It is equipped with the facilities of forty years ago. It can handle a vessel of 250 feet in length, when the lake carrier of today west of Buffalo is 600 feet in length. That means that the carriers that operate on this 40-year-old route are limited in number, and limited more in carrying capacity. Thirty days ago those carriers were operating on a tariff from Buffalo to Montreal of 6 to 7 cents per bushel. Last Saturday 15½ cents was paid for the carriage from Buffalo to Montreal. That is the pressure of grain west of Buffalo seeking an outlet to foreign markets.

The effect of the market rise in prices has been this. In 30 days the foreign price of wheat has advanced 25 cents per bushel, the foreign price of corn has advanced 20 cents per bushel, because these markets are inadequately supplied. The market price in America of wheat has advanced 10 cents per bushel, and of corn 10 cents per bushel. That is, the spread between the ultimate foreign price which should be reflected back to our farms, has widened from 10 to 15 cents per bushel because of the lack of adequate facilities to move the crop pressing on the market in the west.

I make the statement out of 30 years' experience as a grain exporter, watching the diversions of grain from route to route for a half cent per bushel economy of one route against another. As a member of a trade that has been content for years to lift grain from the western primary markets, like Duluth, Port William and Chicago, and deliver it to Hamburg and Rotterdam and Liverpool and London for a charge of one cent per bushel, I make this statement, that we have today four billion bushels of grain in the west, the value of which to the farmer in every market in the west is at least ten cents per bushel below a proper relation with the European consumer markets. You take 10 cents per bushel, assuming this continues through the crop year—and it won't, thank goodness—and it would mean a loss in farm revenues of $400,000,000.

I don't need to tell you business men, familiar with business, what the loss of $400,000,000 of enlarge spending power to the grain farmers alone would mean to other industries of this country.

That train of evil, that train of economic loss to a basic industry of this country, follows, I believe from an over-rigid system of government regulation over our railroad, which has extended over ten or twelve years. By a process of control of revenues without any responsibility for operating costs we have destroyed the earning power of our railroads. We have thereby undermined their credit, and from neither source, of earnings nor of credit, have they been able to maintain their equipment in a proper expansion with the growth of this country.

Conditions at Country Stations

A letter dated Minneapolis, November 8, from a valued correspondent of this paper, describes the situation in part of North Dakota as follows:

One of our collectors in a letter just received stated that he was in a town in western North Dakota where the elevators were filled with wheat and could not take another bushel; that on the day he was there some 148 wagons loaded with wheat and other grains were hauled in by farmers and standing on the street unable to find a market, and that the farmers would have to dump their grain wherever they could find a storing place for it, or haul it back home, but it could not be sold.

I have a letter this morning from a bank in which I am interested in western North Dakota from which I quote: "Collections are at a standstill owing to car shortage. The roads are impassable today owing to heavy rain and snow. We are bending every energy to secure as much liquidation as possible this year. Lots of grain is out of doors yet and where the farmer hauls and disposes of a load at a time, it is difficult to secure the payments we might obtain if all sold in a lump."

We have had very good fall weather which has enabled farmers to get their plowing and cultivating fairly well done, with the exception of a great many tenant farmers who are abandoning their operations entirely moving into cities and manufacturing centers where wages just now are very good and who swear they will never attempt to farm again. This will have a tendency to restrict the crop area very materially for the coming year and may prove something of a blessing to those who continue to farm.

Losses of Dealers and Millers

Dealers have been heavy losers through inability to fill contracts, demurrage charges, etc. The Northwestern Miller says that millers have been paying from 5 to 8, and as high as 15 cents premium for wheat in cars that could be re-routed East with flour, and that they have been employing hundreds of carpenters repairing out-of-order cars in order to utilize them for their shipments.

Esch-Cummins Law

The parties who are moved by these conditions to advocate the repeal of the Esch-Cummins law are probably overlooking the provision in the latter under which the railroad companies earning more than the fair return upon their investment fixed by the Inter-State Commerce Commission are required to pay one-half of the excess into a fund, under the control of the Commission, to be invested in equipment to supplement the regular supply in emergencies such as the present.

Actual Accomplishments

It must not be supposed, however, that the railroads have not been moving large quantities of grain. The receipts of wheat at the twelve "primary markets" from July 1 to November 11, 1922, were 220,605,000 bushels, against 244,975,000 bushels in the corresponding weeks of last year, and of other grains about the same as last year. Exports of United States wheat, including flour as wheat, in October were 18,282,140 bushels against 18,205,966 bushels in October, 1921; same July 1, to October 31, 1922, 114,973,000 bushels, against 161,572,000 corresponding period 1921, and 145,351,000 in 1920.

Furthermore, it must be considered that if all the grain offered at railway stations in last three months had been promptly moved to the terminal market, prices at the latter might not have been sustained at the figures that have ruled, and even Liverpool prices might have been affected.

The railroad companies came into the crop moving season with much motive power in poor condition as a result of the shopmen's strike, and have had to deal with an extra heavy movement of coal, resulting from the coal strike, and with all traffic reviving. In the last week of October, 1,014,480 carloads of freight were loaded, which is but a fraction of one per cent below the peak-loading of any week in the history of the country. The car loading figures for the past month not only exceed those for November, 1921, but are the highest for that month on record.

The Cotton Crop

The ginnings of cotton to November 14 amounted to 8,869,857 running bales, but there is much opinion that the total yield may not reach 10,000,000 bales. The Southern Textile Bulletin offers the following calculation upon the supply and probable demand for cotton to the end of the new crop year:

August 1, 1922, carry-over in the United States	2,828,000
1922 crop	9,800,000
Total supply in the United States	12,628,000
Consumption and exports	12,100,000
In United States August 1, 1923	528,000

This writer estimates domestic consumption and exports at 12,100,000 bales.

Mr. Arthur Richmond Marsh, editor of the Economic World, who is one of the most competent writers about cotton, says that the minimum annual supply of American cotton required to meet the needs of the world's cotton industry as now developed is 13,000,000 bales. The world takings of American cotton in the last crop year, according to Mr. Hester, Secretary of the New Orleans Cotton Exchange, were 12,804,000 bales and consumption was decidedly below normal. Evidently there is danger of a serious scarcity of cotton.

The larming feature of the situation is the fact that this year's acreage preliminary estimate is 34,852,000 acres, against an average of 35,088,200 acres in the ten years ended with 1920, and weather conditions this year have been as good as the average. The average crop of the ten years ended with 1920 was 13,014,200 bales. The fact is thus brought

home that the short crop of this year is due to a low yield per acre, and that this is due to the boll weevil. Mr. Marsh says:

Cotton is already commanding on the great Cotton Exchanges and in the spot markets everywhere a price which is considerably more than double the average pre-war price and nearly two and a half times the lowest price to which it declined during the period of price deflation two years ago, while many of the most competent students of the world's cotton situation are of the opinion that in the comparatively near future the price may easily rise to three or perhaps four times what it customarily was in the earlier years of the present century.

Although the crop is short, it was made at comparatively low cost, and at 25 cents per pound probably represents a better net return to the growers than any crop made in the years of higher prices. It assures good business conditions in the South.

The British cotton-goods industry improved very decidedly in the first six months of the year, but of late orders have fallen off. The change is attributed in part to the disturbance in Turkey, and increased pessimism in Europe. Edward T. Pickard, chief of the Textile Division, Bureau of Foreign and Domestic Commerce, returned in October from a trip of observation through Europe. He found the greatest unemployment and pessimism in England. He says:

It is interesting to note that in the minds of Manchester manufacturers and merchants the condition of the American cotton crop, its estimated yield, and even the price, were subjects subsidiary to those conditions of broad political significance, such as reparations, unbalanced European budgets, and the violent fluctuations in exchange. The current of popular sentiment is for a prompt settlement on a reasonable basis of these vexing questions affecting the economic stability of Europe.

He found the French cotton industry in the best state it has been in since the war, and the Polish mills busy. He is disposed to think, however, that Europe will not reach its pre-war consumption of cotton for a number of years.

Our own cotton goods exports have been increasing this year, running in the first nine months about 14 per cent in yardage above the corresponding period of last year. Of last year's consumption of American cotton, domestic mills used 6,234,000 bales and foreign mills, 6,570,000 bales.

Live Stock Markets

The beef cattle markets have been suffering from too many half-finished cattle, but prime corn-fed cattle have been bringing good prices.

The runs of grass cattle from the ranges have been very heavy. Clay's Review says that "Kansas City's October run of 480,600 was the largest month's supply of cattle and calves in the history of any market—and they were largely grassers."

One explanation of Kansas City's heavy receipts is the great drought that has been prevailing in Western Texas, New Mexico and Arizona, which has forced the movement of many herds and been disastrous to the cattle interests. The situation is so grave that arrangements have been made for the removal of many thousands of cattle into Mexico, where there is plenty of grass and water. The herds of Mexico have been much depleted in the last ten years. An obstacle to this policy was encountered in the fact that most of the cattle are under mortgages. A Texas paper speaks of the situation as follows:

Most of the 50,000 cattle to enter Mexico from ranges in West Texas territory will be branded again before they leave this country according to Lee Bell, inspector for the Texas and Southwestern Cattle Raisers' Association. Each animal will bear its own herd brand, he said, and in addition will bear a brand showing that a mortgage is held on it by the War Finance Corporation. Most of the cattle are mortgaged.

American cowboys will accompany the stock into Mexico, but they will act as overseers, and the cattlemen will hire Mexicans in large numbers to guard the stock. This has been promised to Gov. Ignacio Enriquez, of Chihuahua, in making terms to have the stock shipped into that state for grazing purposes.

The cattle, according to Inspector Bell, will be branded in chutes, because most of them are too poor to stand being thrown to the ground and branded.

The cowboys will take their own "shooting irons" into Mexico to protect their herds.

The stocker and feeder movement, which consists of shipments of young cattle and steers suitable for fattening, from the central markets out to the farms, has been on a very large scale, and at much better prices than last year. John Clay & Co. says of it in their issue for November 16:

Some 85,000 more feeding cattle went back to farms from our central markets the past ten months than a year ago—and at $3 to $5 per head greater cost.

In the same period 420,000 more sheep and lambs went back—at almost double last year's cost.

Reasoning from this to probable supplies of beef cattle next spring and summer, they say:

There will be all the cattle the markets can absorb during the next seven or eight months, but after that the unusual jettisoning of supplies this fall will be felt and apparent in light range runs. Should the trade give a good account of itself meanwhile, and we believe it will, the range cattle man should have his inning next fall. But that's a long time for a man near drowning to keep his head above water.

Conditions in the South

The report of the Federal Reserve Bank of Dallas, dated November 1, 1922, describes general business conditions in that territory as follows:

Not since the winter of 1919-20 has the activity of trade in the Eleventh District shown as great a buoyancy as it displayed during the month of September, 1922 * * * Collections, after months of sluggish movements, showed marked improvement in September, due chiefly to the large volume of money put into circulation recently by the marketing, at satisfactory prices, of the district's cotton crop.

Financial conditions in this district now present a most unusual situation. The extent to which in-

debtedness (both personal and corporate) has been liquidated during the past year is partially reflected in the fact that our loans to member banks have been reduced during the twelve months ending October 18 from $68,000,000 to $21,000,000, or approximately 70 per cent. Both the Federal Reserve Bank of Dallas and many of the commercial banks of the district have been forced to enter the open market to obtain employment the large surpluses of idle funds—a condition practically unprecedented for this season of the year.

The following extract from a letter dated November 13, from a well-informed banker in Mississippi, describes present conditions in that state:

Present conditions in Mississippi are very satisfactory. This State will probably rank second in the production of cotton. Prior to November 1st the ginnings ran eight hundred and sixty odd thousand bale, and we estimate our total crop around one million to one million one hundred thousand bales. At the prevailing prices, this crop is bringing a great deal of money into the State and many old debts have been liquidated and trade is very good—both wholesale and retail. The crop was very economically produced and this is a prime factor in the improvement of conditions. Feed crops, such as corn, hay, etc., are very satisfactory.

In South Mississippi the lumber interests are enjoying a good business, their shipments at fair prices being limited, however, by car shortage. Generally speaking, the lumber manufacturers are in good financial condition. Our chief monied crop, by all odds, is cotton; second lumber; third cattle and hogs. Livestock has not been very satisfactory and most of the farmers are declining to sell their livestock at the present market and are holding for higher prices.

Corporation Surplus

The agitation, for the taxation of corporation surplus or stock dividends representing transfers from surplus account to capital account, has been revived, and is at once the cause and result of numerous stock dividends recently. The announcements of these dividends, which under a decision of the U. S. Supreme Court are non-taxable for the very good reason that they do not transfer anything, has excited a portion of the public, which understands them to be a distribution of profits, and prompted a demand for more taxation. On the other hand, the revival of the demand for the taxation of such surplus or stock has naturally prompted corporations to complete any action of the kind they may have been contemplating.

What Is a Surplus?

It is not strange that many people should be unfamiliar with corporation finance, in which the term "surplus" is used in a technical sense. In the case of a corporation it does not mean cash on hand or an excess of any kind of assets over its needs, but simply an excess over the sum of obligations and capital stock outstanding. The "surplus" shown in a corporation's statement may be, and commonly is, all invested in buildings, machinery, and necessary working capital. In the operation of the business it is indistinguishable from that part of the capital represented by capital stock.

An individual in an unincorporated business does not have surplus in the same technical sense, nor does a partnership, because they have no outstanding stock. They do not ordinarily make the distinction between "capital," "surplus" and "undivided profits" that is done in corporation bookkeeping.

When it comes to taxation, individual proprietors and members of partnerships pay the regular personal income taxes upon that portion of the profits of the business which belongs to them, whether they withdraw any part of it from the business or not, and that is all the taxes paid upon those profits. The profits are counted as income to the proprietors once, and that is all.

The Corporate Organization

The foregoing is something to bear in mind in considering what is just and fair treatment as between persons who choose to carry on business under the corporate form and those who carry on perhaps the same kinds of business as individual proprietors or in partnerships. From the standpoint of public policy. there is no good reason why the Government should discriminate against the corporate form of proprietorship. It is the greatest agency in existence for the widespread distribution of the ownership of large undertakings. It is the most practicable means available for promoting co-operative industry on a large scale. It has become common practice for corporations operating public utilities to sell their new stock issues to their patrons and employes, a notable example of such distribution being the case of the American Telephone and Telegraph Company, which has over 235,000 stockholders, of whom over 46,000 are telephone employes.

Although a great portion of the business of the country is carried on by individual proprietors and partnerships, in many lines the operations are of such magnitude, requiring so great an investment of capital, that they cannot be handled economically and for the best service of the public except by corporations. It is not desirable that the development of industries on a large scale shall be limited to individuals rich enough to own them alone or in partnership with a few others. The joint stock corporation has opened the way for general participation in industry on a large scale.

Even in the case of small enterprises, there are advantages on the side of corporate organization. Thousands of such organizations operate laundries, creameries, grain elevators, retail stores, small factories and other concerns in which it is desired to have many persons interested in the business.

We repeat that there is no good reason why the persons desiring to conduct any business,

whether large or small, under the corporate form of ownership, should be placed by policies of the Government under any burden or disadvantage as compared with individual proprietors or partnerships. They are entitled to like consideration and similar treatment.

Personal and Corporate Taxation

As we have seen, individual proprietors and partnerships are taxed upon their profits once for all, and afterward may leave them in the business or take the amount, as they please. Their taxable incomes (in excess of personal exemption for normal tax) to the extent of $4,000 per year are taxed 4 per cent, and above $4,000 bear a normal tax of 8 per cent, and the regular surtaxes. The corporation is taxed 12½ per cent upon its taxable income, and any distribution of that income to its individual stockholders is taxed again upon the same basis, for surtax, as the income of individual proprietors and partnerships. In other words the effect is this: parties doing business as a corporation pay a 12½ per cent tax on the net earnings of the business instead of the 4 per cent or 8 per cent normal tax which individual proprietors and partnerships pay, and the same surtaxes as the latter, upon all their income from the corporation dividends.

Although it is argued that a corporation is an entity, and as such properly subject to taxation independent of its stockholders, it is evident that all taxes paid by a corporation come out of earnings that are destined for the stockholders, and while moderate taxes may be justified as compensation for corporate privileges, it is evident that they involve double taxation, and to that extent penalize the use of the corporate organization. Moreover, heavy taxation of corporation earnings are inconsistent with the whole scheme of graduated taxation for they fall at the same rate upon stockholders with small incomes as upon stockholders with large incomes. The present 12½ per cent tax on corporation incomes is a heavier tax than many shareholders would have to pay if they received their portion of the earnings from a partnership instead of from a corporation, and that discrimination will be made greater if corporate taxes are increased.

The "surplus", or undistributed profits of corporations equitably belongs in due proportions to the small and large stockholders according to their holdings. The individual proprietor or member of a partnership withdraws profits from the business or not, as suits the case, but has paid the surtax to which he is subject. The corporation pays 12½ per cent, but no surtaxes, for the reason already shown, i. e., the imposition of graduated surtaxes upon corporations would be manifestly unfair to the small stockholder or the stockholder of small income. There are many stockholders in the United States Steel Corporation and every large corporation whose total incomes do not make them subject to surtaxes. If the graduated scheme of taxation is right, heavy taxes upon corporation earnings or surplus are all wrong. The profits of corporations should be taxed as they are distributed to the stockholders, according to the total incomes of the several stockholders.

The Law Regarding Surplus

The argument for the taxation of corporation surplus is that if corporations were permitted to accumulate earnings in their treasuries indefinitely, or to invest them outside of the business, the stockholders subject to surtaxes would escape the payment of them so long as this policy was followed. Whenever the distribution of corporate earnings occurred they would be liable for the surtaxes, but the distribution might be postponed.

On the other hand, it would not be desirable to compel corporations indiscriminately to divide all their earnings promptly. Every growing business is constantly requiring more capital, and it is the common practice, not only of corporations but of individuals and partnerships, to allow a portion of their earnings to remain in the business each year for its development. The history of nearly every important business will show that it was built up in great degree by so doing, and it would be a serious handicap upon the corporate form of organization if it was not given the privilege of building up by this method. Moreover, it always has been regarded as sound, conservative and praiseworthy policy for a corporation to build up a surplus account—representing surplus assets—over and above the amount required to cover its obligations and outstanding capital stock. The position of the corporation as an industrial institution, as an employer of labor, as a borrower of money, as a supporter of trade, as a factor in many ways in the regular life of the community, is strengthened by the policy.

It appears that Congress took these facts into consideration and did not intend to interfere with the normal and proper management of business. In order, however, to provide against accumulations of "surplus" for which there is no legitimate use, and which there is good reason to believe are held for the purpose of escaping or postponing the application of the individual surtaxes the revenue act of 1921, section 220, provides as follows:

That if any corporation, however created or organized, as formed or availed of for the purpose of preventing the imposition of the surtax upon its stockholders or members through the medium of permitting its gains and profits to accumulate instead of

being divided or distributed, there shall be levied, collected, and paid for each taxable year upon the net income of such corporation a tax equal to 25 per centum of the amount thereof, which shall be in addition to the tax imposed by section 230 of this title. * * *

The fact that any corporation is a mere holding company, or that the gains and profits are permitted to accumulate beyond the reasonable needs of the business, shall be prima facie evidence of a purpose to escape the surtax; but the fact that the gains and profits are in any case permitted to accumulate and become surplus shall not be construed as evidence of a purpose to escape the tax in such case unless the Commissioner certifies that in his opinion such accumulation is unreasonable for the purposes of the business.

Impossible to Distribute Invested Surplus

If legislation is adopted for the taxation of corporate surplus as such, it is bound to have one of two effects: It will either sacrifice unjustly the interests of the stockholders whose total incomes do not make them properly subject to this further levy, or it will force the distribution of the surplus in cash, which is practically impossible in the numerous cases where the surplus has been accumulating for many years, and is invested in plant and working capital needed in current operations. In either case the legislation would cause disaster. A tax levied upon surplus would be retroactive, reaching back into what was left from the taxation of all previous years. It does not seem possible that Congress will seriously consider such a proposal, but evidently not a few members of the next Congress are considering it.

Stock Dividends

Although in the case of a new company a surplus account is sometimes started by the sale of stock at a premium, a corporation surplus usually consists of undivided earnings, accumulated over a term of years, and, as stated above, does not exist in cash but in the plant or working capital. It buttresses and protects the regular capital behind the issued stock, preventing its impairment by unexpected losses, and this is one reason why it is considered wise policy to pay in a moderate surplus with new capital.

If a business is growing it will need more capital and the readiest way of providing it is by allowing profits to accumulate from year to year. If the opportunities for expansion are good, it is often the case that only a small share of the earnings are divided, and not infrequently companies go for years without paying any dividends in order to apply all the profits to developing the business or getting it into a strong financial position.

In the long run, however, stockholders want to participate in the company's prosperity in a tangible manner, and where the stock is widely distributed a proper consideration for the varied circumstances of the holders dictates that regular dividends be paid and that the distribution be increased from time to time as the company's assets and earnings increase. This is consistent, however, with the policy of continually retaining a part of the earnings.

When the condition of the company justifies an increased distribution to stockholders, the action seldom applies to anything but current earnings. A growing business does not distribute surplus which is part of its working capital. It may raise the dividend rate on its outstanding stock, or it may convert a portion of the "surplus" fund into permanent capital by means of what is called a "stock dividend." This is done by issuing to stockholders a given amount of new stock, in proportion to their holdings, and making a bookkeeping entry by which the "surplus" fund is reduced and the "capital" fund is increased to correspond with the amount of new stock.

Not a Real Dividend

The fact that such an issue of stock is called a "dividend" seems to have led many persons to think it a payment from the treasury of the company, similar to a cash dividend. It is nothing of the kind. It is not a payment; it is not a distribution. It conveys no title to anything that the recipient did not own before. Nothing is changed, except that the stockholder's share of the surplus has been changed on the books of the company into capital, and he is given a stock certificate representing that capital. The company's assets are just what they were before and each stockholder's interest in them is just what it was before. No value has been created or distributed. There is no more reason for levying a tax upon the conversion of "surplus" into "capital" than for levying a tax on the opening of a new set of books. In fact "surplus" is part of a corporation's capital. A stock dividend dedicates it permanently to the business.

The Supreme Court of the United States, in the case of Eisner v. Macomber, 252 U. S. 189, in which it held that stock dividends were not liable for taxation as income under the law, said:

This, however (declaration of a stock dividend), is merely bookkeeping that does not affect the aggregate assets of the corporation or its outstanding liabilities; * * * it does not alter the preexisting proportionate interest of any stockholder or increase the intrinsic value of his holding or of the aggregate holdings of the other stockholders as they stood before. The new certificates simply increae the number of the shares, with consequent dilution of the value of each share.

The difference to the stockholder is in the fact that while "surplus" does not receive dividends, "capital" does, and the new stock is evidence of a claim for dividends in the future. This, however, is a difference in method rather than in fact, because just as much could be distributed in dividends on the old stock as on the new. If a company with $100,000 capital

and $100,000 surplus pays six per cent dividends it distributes $6,000. If it wants to increase the distribution to $12,000, it can do so by either increasing the dividend rate to 12 per cent or by converting the $100,000 surplus into capital and continuing to pay 6 per cent on the $200,000 capital.

A stock dividend is usually a preparatory step to a larger distribution of earnings in the future. The distribution, however, may not begin at once. Sometimes the rate of cash dividends is reduced, so that the amount of money received by the stockholders is no greater than before the new stock was issued. Whenever the actual distribution of earnings to stockholders begins the payments are taxed under the present law. It looks like an excess of zeal to insist upon taxing a preliminary arrangement.

Not Stock Watering

The issuance of new stock by the conversion of surplus is sometimes called "watering" the stock, but this is not according to the common and opprobrious meaning of the term. It is true that the value of the outstanding stock is reduced to correspond with the increased issue, but it is not true that the new stock has nothing behind it. If paid for from accumulated earnings which stockholders have abstained from withdrawing from the treasury it is as fully covered as the stock issued against payments into the treasury.

The Motive

If the new stock issues transfer no values, represent no values that did not exist before, and give no claims to dividends that might not be paid upon the old stock, why are they issued and why do stocks advance on the market upon rumors that stock dividends will be declared?

One reason is that an announcement of a stock dividend is usually accepted as signifying that the company is in position to increase its regular distribution to stockholders, and news of that kind is usually pleasing. The public, as a rule, does not enjoy waiting for benefits, and the fact that a company is earning 12 per cent dividends, but paying only 6, retaining 6 for enlarging the business, does not make as good an impression as the announcement that henceforth it will pay 12. It is the same impatience which causes some legislators to insist upon the payment of 12 instead of 6 under the same circumstances, in order that the stockholders may have to pay higher taxes. The sagacious stockholder will reflect that the retention of the 6 per cent for the enlargement of the business means larger earnings and dividends in the future, and the sagacious legislator will reflect that by the same logic it means larger revenues to the public treasury in the future, but impatient stockholders and impatient legislators alike cannot bear to wait. It is the same old impatience that always has impelled people to eat the seed corn rather than plant it in the ground.

A stock that has a high surplus value but is paying a relatively low dividend will not as a rule have as high a market value as one that has a low surplus value but is paying a relatively high dividend. In other words, the inclination of the public to rate immediate realization relatively higher than future realization tends to make stocks rise on the expectation of increased distribution.

Moreover, a stock with a high surplus value becomes unattractive to many possible buyers because the price looks so high, and they are able to buy but few shares. One of the old banks of New York followed for many years the policy of allowing earnings to accumulate until its shares became worth about $3,500 each. Of course such a value is not favorable to a wide distribution of the stock. The book value of the capital stock of the Ford Motor Company, according to its statement of June 30, 1922, was about $1,780 for each $100 share. If the present owners should think it desirable to invite the public to participate, no doubt that would be best accomplished by issuing more shares against the accumulated surplus, thus reducing the value per share. One of the reasons given by the Standard Oil Company of New Jersey for its recent conversion of surplus into capital was that it has adopted a plan for inviting a participation of its employes in the ownership. Many companies, including the one last named have reduced the par value of their stocks to $25 for this purpose. They are more readily purchased by persons of moderate incomes. The stocks of low book values sell relatively higher than those of high book values, and announcement of changes in this respect affect market prices.

No Evasion of Taxation

It will be seen that there is nothing in the accumulation of a legitimate corporation surplus, or in the declaration of a stock dividend that is in evasion of the law or that accomplishes any permanent escape from taxation. Upon all corporation profits above the exemption of $2,000 when profits do not exceed $25,000—no exemption above—an income tax of 12½ per cent is no wpaid, whether they are retained or distributed, and whenever any actual distribution to stockholders takes place the latter must pay the income surtaxes to which they are subject. If the earnings of corporations are retained for use in the business, they will accumulate and yield more taxes whenever distribution occurs. They are practically money at interest for the govern-

ment, for they are bound to become subject to the personal taxes sooner or later, if the stockholders or their heirs ever get anything from them.

The Standard Oil Company of New Jersey

One of the cases illustrating the capitalization of surplus that has been featured lately has been that of the Standard Oil Company of New Jersey, which has declared a stock dividend of 400 per cent. This company has long been the leader in the oil business in volume of business done, although in recent years the number of oil companies has been multiplied over and over again, and the percentage of the business done by companies unrelated to the Standard companies has greatly increased.

The volume of business done by this company runs into figures which seem staggering to many readers. As in other instances where the profits of big business are stated, some people fail to take account of the magnitude of the volume of business done and of the fact that the profits are no greater in proportion to the aggregate of the transactions than are common in relatively small business.

In a statement announcing to the stockholders of the Standard Oil Company (N. J.) the purpose to make the pending stock issue, Mr. A. C. Bedford, Chairman of the Board, said that throughout the twenty-three years since 1899, it has been the policy of the company to reinvest in its business all its earnings remaining after the distribution of "dividends," and that since the year 1911 there had been no increase in the dividend rate, which has been 5 per cent. It is evident that thus compounded the surplus would grow rapidly in the latter years of the period, particularly in view of the great expansion the oil business has had in these years. This surplus, he says, is now represented in the balance sheet by refineries, pipe lines, steamships, raw and finished products, and other investments in property both in this country and abroad. That portion represented in cash is a relatively small portion required for the current needs of the business. He analyzes the earnings in recent years as follows:

> In ten years from 1912 to 1921 inclusive, the company has shown net earnings before taxes of $775,163,260. Of this considerable sum, $115,517,677 has been paid to the Government for taxes, $222,065,226 represents aggregate dividends for the period, and $437,580,357 has been absorbed by the needs of the business referred to.
>
> Large as these earning seem as expressed in dollars, they have during the past ten years averaged only 12.76 per cent on the company's investment—a rate of return certainly not in excess of that considered essential to the prosperity of a speculative business of this character. During the same period, the common stockholders have received in dividends 30 per cent of the company's aggregate net earnings.
>
> Another point of importance is that every dollar of the earnings of the company has been subjected to all taxes applicable—income, excess profits, and others, both at home and abroad. During the ten year period mentioned, the Standard Oil Company (N. J.) has paid to the United States Government alone, taxes amounting to $115,517,677, or 14 per cent of its total net earnings. The years of highest excess profits taxes required such heavy payments on this account that the company was deprived of its normal sources of new capital and, to finance the natural expansion of it business, found it necessary to create and sell to the public two issues of its preferred stock.

The two issues of preferred stock to which this statement refers aggregated approximately $200,000,000, and were sold in 1911 and 1920. These sales of stock for the purpose of raising capital, afford the best possible evidence that the company has not been accumulating surplus in excess of the needs of its business.

Growth of the Petroleum Industry

The explanation of the accumulation of surplus and sale of stock to raise capital is to be found in the rapid development of the petroleum industry. No longer ago than 1900 the total production of petroleum in the United States was 63,620,520 barrels, but in 1921 the marketed production, as reoorted by the Geological Survey was 469,639,000 barrels. This expansion of the industry required a great increase of the facilities for moving, storing, refining and distributing oil, and the companies that promptly provided these facilities handled a large volume of business. Standard Oil has been a pioneer in the development of petroleum products, and this company with a marketing system that extended over the world has been the leading factor in the distribution of the rapidly growing output.

The taxes paid, as stated by the Chairman, are only those paid upon the earnings of the company, not including those paid by the stockholders as earnings were distributed. Moreover, the retention of a part of the earnings in each year has had the effect of increasing the earnings and taxes in each and every following year, at the compound rate of increase. In other words, the Government has participated in the increased earnings resulting from the company's policy.

Standard Oil and Ford Motor Companies

Standard Oil is eminent in one industry as the Ford Motor Company is in another, although in profits upon invested capital the latter has far outstripped the former. They afford the most striking illustrations of great business built up by reinvesting and compounding the earnings. In both cases the results have become largely due to the phenomenal growth of the public demand for the products, and to a great extent it has been a closely related expansion, for the growth of the automobile industry has been dependent upon the development of the oil industry, and the oil industry has been enormously stimulated by

the development of the automobile. In the last twenty years they have developed together, and to accomplish that development, by the reinvestment of earnings, either by oil companies or automobile companies, has not been a policy harmful to the public. Neither company could have played the part that it has in the expansion of the industry, or paid the taxes that it has, if it had not been allowed to accumulate and capitalize earnings. And the properties that have been built up in each case are certain to be great revenue-producers to the Government for years to come.

The Popular Error

The popular error which is responsible for the demand for the distribution of corporation surpluses, as in all the schemes for leveling society, is in thinking of these accumulations as not only privately owned but devoted to private purposes. They are privately owned, but so long as they remain as they are they are devoted to public purposes—the production of things wanted by the public. An organization producing goods or services for the public market, which never distributed any profits to its owners, but used all its earnings to provide capacity for satisfying an increasing public demand, could not serve the public more completely if it was owned by the Government—and judging by all experience probably would not serve it nearly so well.

If the Government had taken over the automobile and oil industries twenty years ago, and the Government officials had been clever enough to have accomplished the same development that these proprietors have accomplished, they would have had to raise practically the same amount of new capital that the private proprietors have found and invested. The latter have gotten the capital out of the industries, and the Government could have gotten it in no better way.

Down to this point, then, there doesn't appear to be any real ground for complaint of what these private proprietors have done. They have been wideawake and enterprising in supplying certain public demands. If it should be said that they might have been satisfied with smaller profits, the answer is that if profits had been lower the expansion of the industry would have been slower, the supply of products would have been smaller, and prices would have been higher instead of lower. Prices are not fixed arbitrarily, and the best price for both producers and consumers is the price at which demand and supply meet—the price that clears the market. If the market is above that, a portion of the product is unsold, and if below, the wants of the public cannot be fully met.

It will be said, probably, that this is all very well so far, but that these great properties, thus created, belong to the proprietors, and that whenever the latter choose to change this policy of devoting profits to production they can do so, and proceed to withdraw, divide and consume the earnings thereafter. That is true, and is the very point to which we are directing attention. It is only when private capital ceases to be capital, ceases to be used productively, and is converted into something to be consumed by the owners, that its employment for public purposes ceases.

This being so, what logic is there in disturbing a corporation surplus which is employed in a productive industry, for the purpose of forcing it out of that employment into the hands of the individual shareholders? The policy would be disruptive of the industrial organization, and while it would procure immediate funds for the treasury it would be taking funds from a public use, rather than, as fancied by the advocates of the policy, from the service of the owners.

The Ford Policies

Mr. Ford is quoted as saying that he believes the best use he can make of his profits is to invest them so that they will give work to more people, and this view is essentially sound. According to the last statement of the Ford Motor Company its capital stock was $17,264,500, its surplus $289,935,296, and its reserves for income taxes (half way through the year) were $44,848,893. Evidently the ability of the company to give employment to 100,000 or more workmen exists chiefly in the surplus and that part of the capital which represents conversion from surplus. Evidently, also, the company is paying very large taxes now. Looking back over the record, at which stage would it have been advantageous to the public to have stopped the development of this business?

When this question is answered as to the Ford Motor Company it is answered as to all other companies, for they all accumulate surplus for the same purposes, and use them to build larger factories, buy more machinery, employ more labor and turn out increasing quantities of things wanted by the public.

Does the fact that Mr. Ford is a leader in the payment of high wages affect the economic principles involved? We think not. If high wages are paid as a matter of business policy, because they result in the lowest unit costs, there is no room for argument over the policy. Every employer wants the lowest cost of production and to be able to employ the greatest possible number of men. It is useless to insist that every employer shall have the genius for management of Henry Ford and at the same time quite needless to insist that they shall be as successful as they can be. Taking industry as a whole, wages are fixed by the

volume of production and the law of supply and demand; a policy of increasing wages which does not increase production cannot be general. Having these facts in view, what is the comparative influence upon the labor market between giving employment to 1,000 men at $6 per day or 1,500 men at $4 per day?

Stating the problem differently and assuming that Mr. Ford's wage bonuses were not dictated by business policy and yielded no returns in production, would the policy of bonuses have any greater effect upon the labor market, or be of more benefit to the wage-earning class, than a policy which would distribute the same amount in wages to a greater number of men? The economic influence of any given industry upon the labor market depends upon the numbers of workers it takes off the market.

Or, to put practically the same question in still another way, were the disbursements in the form of wage-payments in excess of current market rates—still assuming that they were not based upon direct economic returns —of greater benefit to the wage-earning class than the profits which Mr. Ford reinvested for the enlargement of the business, for example the $40,000,000 said to have been devoted to the development of the farm tractor?

The Means of Leadership

These comments are made simply to emphasize what we understand to be Mr. Ford's own view, that the best use he can make of his profits is in giving labor to more people. The growing accumulations of capital in Mr. Ford's hands have made him on the one hand a great influence in the labor market and on the other hand a great leader in the improvement of industry and the cheaper production of food stuffs and other things that minister to the wants and comfort of the population. The supply of capital at his command is what makes his leadership in industry effective. What would the people of this country gain by any action at Washington for the purpose of taking Mr. Ford's profits out of his hands as fast as he makes them? Is Washington able to put them to a more advantageous use than he?

If the question is answered as to Mr. Ford it is answered as to every other person or company engaged in productive industry.

Many persons who are admirers of Henry Ford but critics of the existing industrial system, fail to give the system credit for affording the opportunity for Henry Ford, John D. Rockefeller, Andrew Carnegie, Charles M. Schwab, Judge E. H. Gary, and many others, to rise from humble beginnings into the positions in the business world which they have reached, and for which they were so well equipped. These who are named have attained distinction, but every community in the country has men who on a smaller scale are playing a useful part in the effective organization of industry. It is by such leadership that society makes progress.

Taxation a Necessary Evil

It goes without saying that taxes must be high to provide the revenues required to meet the necessary expenses of the government, and the earnings of accumulated wealth must contribute very largely. Nothing herein said is intended to controvert this. It is of great importance, however, that it shall be generally understood that reductions of the working capital of the country make everybody in the country poorer. The wealth employed in industry is social wealth, no matter who owns it. Not until it is withdrawn for private consumption does it cease to yield social benefits. The Soviet revolutionists of Russia had a theory that leadership in industry counted for nothing, and that wealth under private control was of no value to anybody but the owners. They were resolved to bring everyone down to a common level, and had their minds so intently fixed upon distribution that they gave no thought to production. They proceeded to take out of the hands of the leaders of industry the very means by which they were doing their work, and the result has been the most terrible national tragedy of all history. The Soviet leaders have modified their policies very materially in the past year as the result of practical experience. The same old doctrine however is widespread in the United States, and the clamor for increased taxation of wealth is largely by people who favor it as a means of dissipating or distributing the accumulations of wealth that exist. The country will not be safe from such proposals until the fundamental fallacy that runs through all of them is generally understood.

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